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Asset Managers Might Have to Register as MAs.

WASHINGTON — Asset managers may have to register as municipal advisors to protect themselves from violating the Securities and Exchange Commission's MA rule, which restricts non-MAs from giving advice about muni bond proceeds and escrows as well as other financial products commonly used by states and localities.

At issue is the status of asset management companies that are not registered investment advisors under the Investment Advisers Act of 1940. Registered investment advisors are exempt from the MA rule, which otherwise requires any individuals or firms providing advice to state or local governments about the issuance of muni bonds, the investment of muni proceeds, swaps, or muni escrows to register as MAs.

With the July 1 effective date of the MA rule fast approaching, asset managers said they might have to play it safe and register rather than risk violating the rule and facing possible SEC or Financial Industry Regulatory Authority enforcement action because the funds they oversee may contain bond proceeds.

The managers are finding that, because funds become commingled, neither they nor the issuers whose funds they manage are sure whether the funds include bond proceeds or not.

"We're still grappling with the notion," said Matthew Nevins, managing director and associate general counsel for SIFMA's asset management group. Asset managers not registered as investment advisors or as swap advisors with the Commodity Futures Trading Commission had believed they would not be captured by the rule because their primary business is not to handle muni fund proceeds or securities-based swaps, he said.

Asset managers are also concerned about the issue of pooled investment vehicles, which can include muni bond proceeds. Nevins said asset companies are having difficulty determining if these pools contain bond proceeds and therefore are requiring their manager to register as an MA.

"Very difficult to prove," Nevins said of determining whether a given fund contains muni bond proceeds. "Very cumbersome for our managers."

SIFMA sent a letter to the SEC earlier this year asking that it either grandfather all existing investment vehicles and grant them an exemption, or allow a "good faith effort" to suffice in determining if they include municipal bond proceeds or not. SIFMA is hopeful that additional guidance on the rule, which the SEC has said it aims to release prior to July 1, will clear the matter up. If not, Nevins said, asset management companies may have to just register as MAs.

"If things stay the way they are, I think the answer is yes," Nevins said when asked if asset managers will be forced to submit MA registration paperwork. "Their default is going to be just to register," agreed Leslie Norwood, SIFMA managing director, associate general counsel, and co-head of municipal securities.

Victor Siclari, assistant general counsel and managing director at BNY Mellon said his bank established a separate division as a registered MA because there was no alternative. The exemptions available under the MA rule are not sufficient protection for firms placed in this position, Siclari said.

The rule would allow an asset management firm to give advice about muni proceeds if the issuer had retained and certified that it would rely on its own MA, but Siclari said that exemption probably would not be available often enough.

Some market participants have questioned why asset managers placed in this position do not either route such business through a registered investment advisor arm of their businesses, or register as investment advisors themselves. But RIAs typically operate under a totally different fee and organizational structure that could not just be changed to solve the problem, Nevins said. "There is no escape valve here," he said.

Nevins added that asset managers are already highly-regulated by the states they operate in and are often already bound by a strict federal fiduciary duty to put their clients' interests ahead of their own, as an MA is required to do. This duty is imposed on RIAs by the Employee Retirement Income Security Act if they handle retirement or pension funds.

Asset managers have asked municipalities to certify whether certain funds includes muni proceeds, but New York City finance director Alan Anders said issuers would probably not be comfortable with that idea. Issuers have often been spooked by legal communications from bankers in the past. "Many of them are going to be confused, and resist it until it's explained to them pretty clearly," Anders said. A lot of issuers don't even know where their bond proceeds are, sources said.

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